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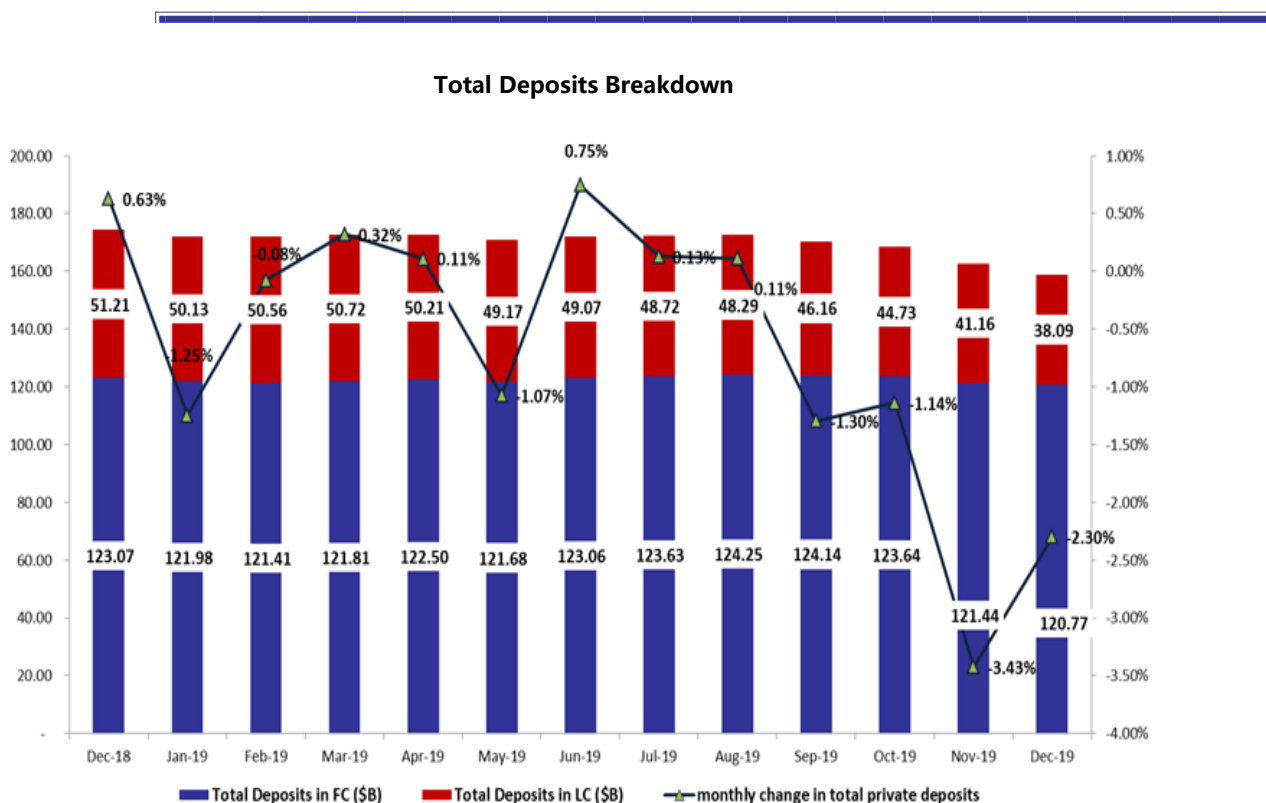
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**Abstract**

According to the consolidated balance sheet of Lebanese banks, total deposits dropped yearly by 8.50% (\$15B) to reach \$162.37B in December 2019. However contrary to recent evidence, this large amount (\$15B) is not entirely an outflow out of the banking system because various sub-components underlying these deposits have also changed over the period. This paper aims to study the relation between the deposits at Lebanese banks and how they are linked to changes in the total loans offered by the banking sector. Moreover, the paper traces the recent, insightful changes in lending to the "Real Estate" (RE) account, as reflected in the performance of Lebanon's real estate sector since the eruption of protests in October 2019 and the imposition of capital controls. Therefore, the study focuses on the critical period between end-September to end-December 2019 to evaluate deposits, loans and the real estate sector mainly through the performance of *Solidere* shares.

**Total deposits dropped by \$11.18B from September 2019 to December 2019 to reach \$162.37B in December 2019.** In details, these deposits include resident and non-resident customers' deposits in addition to public sectors' deposits. From September to December 2019, the highest monthly drop in total deposits was recorded during November by 3.36% (\$5.76B) where the resident and non-resident customers' deposits decreased by \$3.31B and \$2.36B, respectively.



Source: BLOMInvest Bank; Banque du Liban

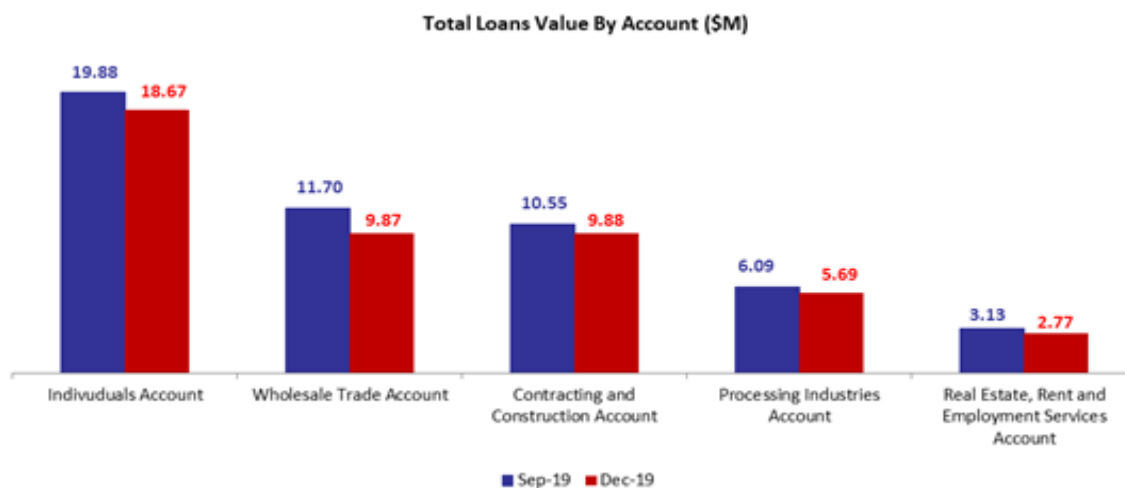
**Since October 2019, the financial crisis has triggered a run on the dollar deposits.** In fact, customers tried to withdraw their money from their deposit accounts amid the fear that the banks might become insolvent. However, while some depositors preferred to transfer their money abroad or even to keep cash money (which is reflected in the significant rise in currency in circulation), others preferred to use their frozen assets and pay back their loans or even buy fixed assets such as properties and real estates which was reflected in the drop in utilized loans.

**The drop in utilized loans was due to different developments.** First, the Lebanese economy has been struggling in 2019 due to low confidence, high interest rates, tight monetary policy and a substantial contraction in economic activity across most sectors which led to a drop in investments and therefore in loans to private sectors. Second, following the eruption of the social protests in October 2019, 5 main market developments threatened citizens' savings and scared away investors:

1. **The imposition of capital controls**, which obstructed depositors' cash withdrawal and transfer operations. These also prevented/complicated the placing and execution of any new international trades or investments.

2. **The shortage of foreign currencies**, namely of US dollars in the Lebanese banking system. This illiquidity quickly pushed the central bank to support essential imports and ensure (credit) facilities to support small businesses.
3. **A rapidly emerging parallel exchange market** as a result.
4. **Frequent discussions regarding an almost “inevitable” haircut on deposits**, regardless of its form(s) that is yet-to-be agreed upon.
5. **The reduction of interest rates**, and especially as this is tied strongly to low interests now earned on client’ s deposit accounts.

**According to the BDL data, total credit by banks amounted to \$57.66B by December 2019, down by 9.22% (\$5.85B) since September 2019.** The utilized loans<sup>1</sup> extended to all 18 economic sectors in BDL’ s dataset witnessed downticks, except those allocated to the sector of “agriculture, fisheries, & forestry” (constituting 1.3% of the total credit). In details, credit to “Individuals” (inclusive of: housing, consumption, car, credit card loans...) which grasps the highest share (32.4%) decreased by 6.11% (or \$1.21B) since September 2019 to stand at \$18.67B by December 2019. Worth mentioning that all the components of this category recorded a drop in their loans value. Moreover, credit to “wholesale trade” (grasping 17.12% of the total) dropped by 15.61% since September to settle at \$9.87B by December 2019.



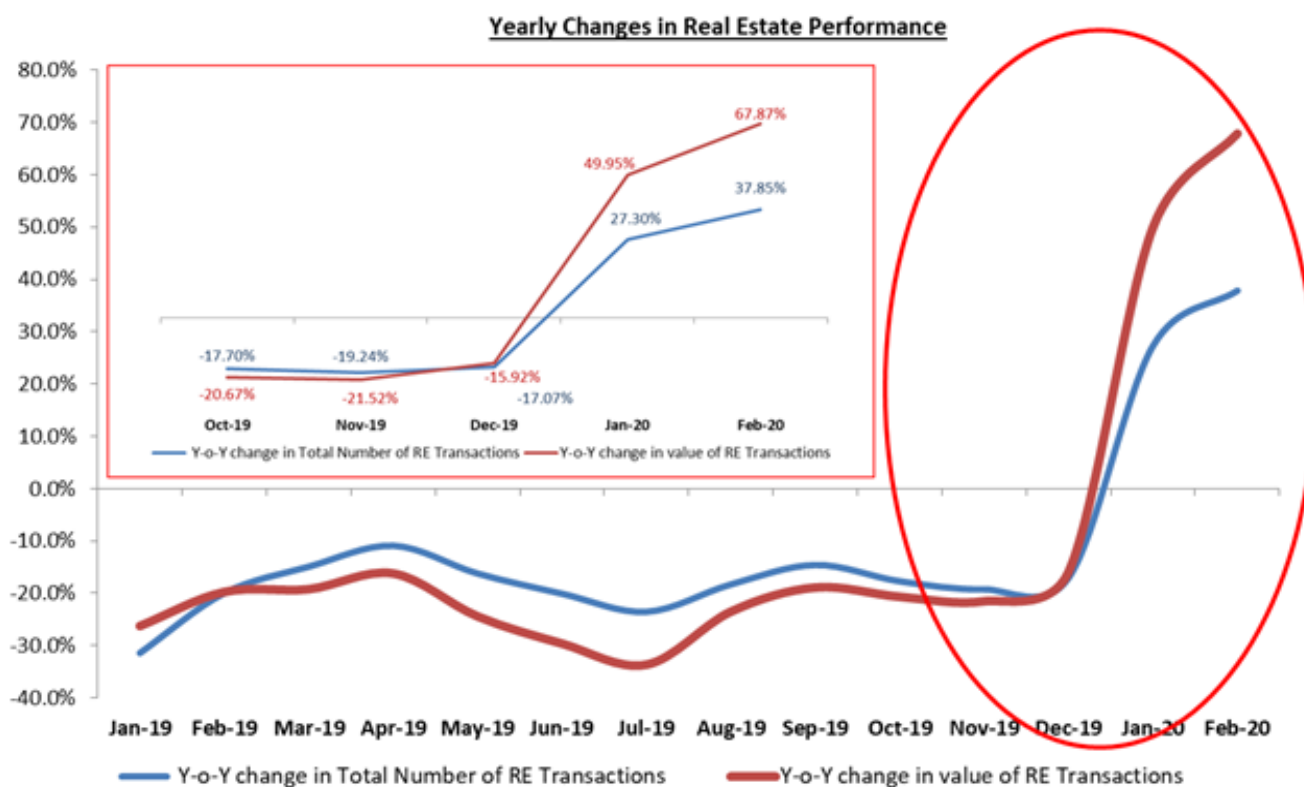
*Source: BlomInvest Bank; BDL*

**Credit to “Real Estate and Construction” combined (constituting 21.9% of the total loans) followed the same trend as real estate developers were ready to sell properties.** In details, the total loans in this

<sup>1</sup> Worth mentioning that these loans are “utilized” and therefore differ from the “total outstanding loans” reflected on banks’ consolidated balance sheet, as the former include the overdrafts.

sector retreated by 7.50% (\$1B) since September 2019 to \$12.65B by the end of 2019. Generally, during an economic recession we expect a drop in investments and therefore a decrease in the value and number of real estate transactions. However, this was not the case in Lebanon. While lending to RE and Construction declined, RE transactions across Lebanon rose starting November 2019. In fact, some of the big depositors at Lebanese banks sought to diversify their investment risk via investing in realties, land and/or properties while contractors took advantage of the situation and payed back their loans by selling their properties.

**The Real estate (RE) sector in Lebanon performed poorly since early 2019; however the downtrend was reversed starting December 2019.** The ensuing data on the Lebanese real estate sector showed that by November 2019, a month after the eruption of the nation-wide civic protests, the number and value of RE transactions suffered further, falling by 19.24% and 21.52% to 44,163 transactions worth \$5.7B, down from 54,687 to stood at \$7.3B by November last year. However, in December 2019 alone, the number of RE transactions (which may include one or more realties) stood at 6189 transactions, almost double November' s. That is to say that an additional 2,889 transactions were executed between November and December 2019, compared to a 16% month-on-month (MOM) decline witnessed in RE transactions between October (the month of protest eruption) and November 2019, with the latter closing at 3,300 transactions.



Source: BlomInvest Bank; Cadastre

**An insightful interpretation of the increased RE demand and declined lending to RE is to trace *Solidere* shares' performance on the BSE.** *Solidere*, one of the country's major land & real estate developers whose properties are mainly located in Beirut Central District, also reduced the size of its own bank loans vis-a-vis solid sales deals signed. In fact, as demand on RE in the Lebanese market rose, *Solidere* was among the market's biggest companies selling more land and/or other owned properties. Doing so, frees the company from the burden of large interest payments that come with big loans weighing down on its profitability and financial position. Moreover, as per *Solidere's* latest public disclosure in 2020, the company had signed sales contracts (deals) worth \$250M in 2019, and by end-February 2020 the signed deals were already valued at a substantial \$112.8M.

It is also key to remember that starting end-November, activity on the Beirut Stock Exchange (BSE) and namely *Solidere's* trades highlighted in this study, was largely affected by the current national political and economic developments, given the Lebanese equity market generally has frail breadth and depth.

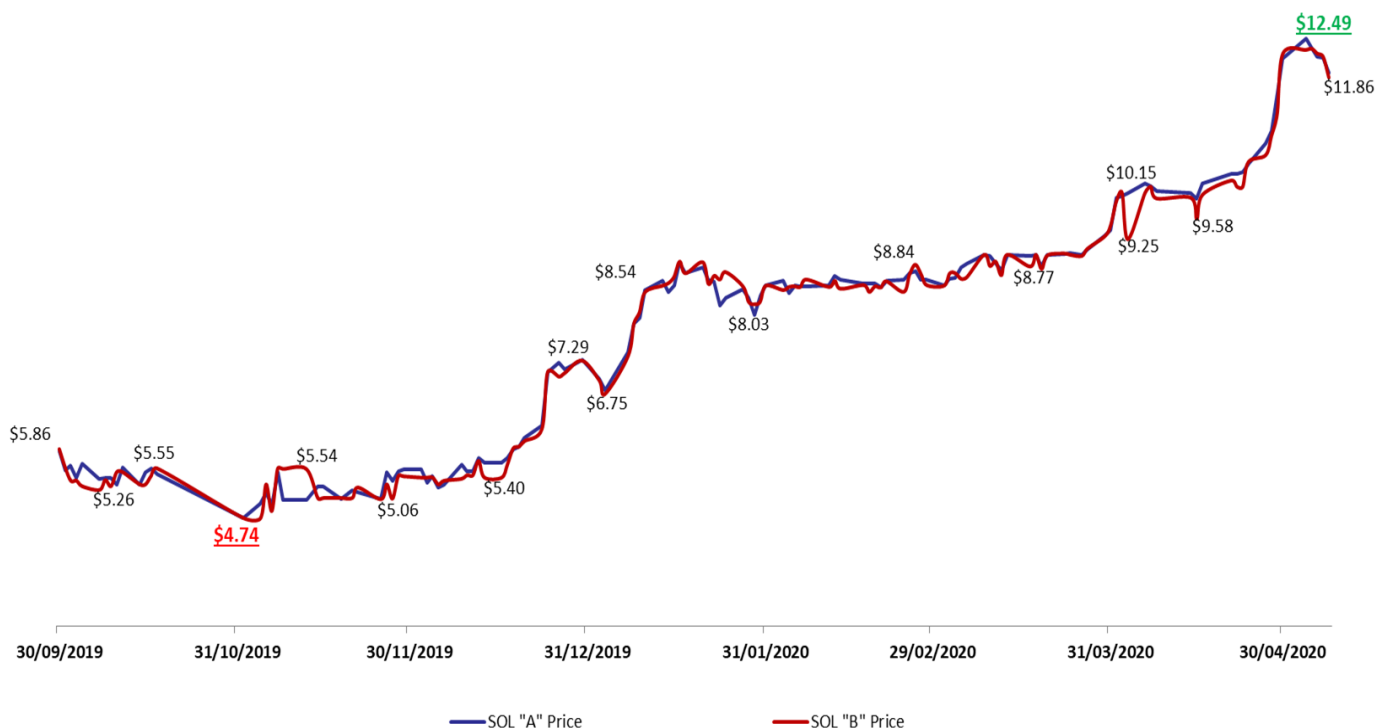
Yet, interestingly, multiple reasons drove up the price and thus the performance of *Solidere* shares on BSE:

1. **Wealthy local depositors freed-up some of their "trapped" bank deposits by buying land and/or property in Lebanon.** Thus, the higher demand pushed real estate prices up, including *Solidere* properties. In fact, the increased demand on Lebanese real estate translated into significant annual upticks of 37.8% and 67.9% recorded in the volume and value of real estate transactions by Feb. 2020 as shown in the previous graph. The RE activity continued its notable uptrend through Q1 2020, as RE transactions totaled 14,068 worth \$2.3B, recording moderate increases of 17% and 44%, respectively, in Q1 2020.
2. **Another viable option for investors with money to spare was to invest directly in *Solidere* shares listed on the BSE.** It is crucial to note that the imposed capital controls did not halt equity transactions within the Lebanese market. In simple terms, some big depositors opted to invest in *Solidere* shares trading on BSE, as they eagerly followed the news on improved corporate profitability. Consequently, some investors jumped on the bandwagon of higher RE demand amid Lebanon's ongoing uncertainty, hoping to reap some profits along the way. **In particular, *Solidere Sal* benefited from increased sales deals (previously explored) which promised to enhance the company's profitability on the medium-term and reduce the corporate's debt-servicing.**

**In fact, the subdued prices of *Solidere* stocks since October 2019 attained an 8-month high in Q1 2020.** Between end-September 2019 and May 04<sup>th</sup> 2020, the prices of *Solidere* "A" and "B" shares added 114.2% and 110.1%, to hit their 8-months highs of \$12.5 and \$12.31, respectively. While the real estate sector overall was grappling with the multi-faceted crisis emerging in Lebanon since the uprising, both shares *Solidere* "B" and "A" had ascended from November 2019's lows of \$4.74 and \$4.75. The

performance of *Solidere* over this period actually mimicked the notable RE downtrend evident during Q4 2019; however the trend was gradually eased starting Q1 2020 as per the graph that follows.

Performance of Solidere Shares on BSE



Source: BLOMInvest Bank; BSE

**Solidere also governed most of the BSE’s trading volume and value amid Lebanon’s developing crisis.** While the upheaval across the country reduced investors’ appetite to invest in the BSE, imposed capital controls and the cloudiness regarding decisions to reform the Lebanese banking sector and restructuring the debt (mainly held by the local financial system) hurt the performance of banks’ shares listed on the stock exchange. On the counterpart, the real estate sector governed most trading sessions over the period. On average, the total volume and value of *Solidere (A & B)* shares composed as little as 19% and 14% of the BSE in Q4 2019, respectively, as the value of BSE averaged \$1.1M. However, by Q1 2020, the average volume and value of *Solidere (A and B)* shares grasped 53% of the average BSE volume in the first three months of 2020 and a substantial 86% of the total BSE value averaging \$732,636 over the same period.

**The prices of *Solidere* shares maintained their Q1 price gains by April.** More recently, Solidere A and B shares respectively ended the month of April 2020 at monthly highs of \$12.17 and \$12.25 per share. However, *Solidere* shares on average grasped only 8.7% of total BSE trading volume during the month as trading on bank shares partially picked up in tandem with most banks’ ongoing cash contribution to

capital (CCC). Meanwhile, the average value of *Solidere* trades constituted 40.8% of BSE' s value which averaged \$1.4M during April.

**However, the more interesting evidence lies within the country' s Construction sector, not RE.** The improved *Solidere* and overall RE transactions pick-up strictly reflect the operations of big depositors who continue to diversify their holdings. Therefore, these transactions do not translate into "real GDP growth" but remain a "synthetic boost" to the RE sector. The depositors' appetite for realties which drove Lebanon' s major listed real estate shares (*Solidere' s*) during Q1 2020 resulted in a sectorial uptrend in the Lebanese RE market since end-November 2019. This is made evident as the number of newly built projects - best captured by the Lebanese order of engineers' data on construction permits - reveals evident slumps of 29.7% and 64.4% in the number and value of new construction projects to 591 permits with a construction area of \$178,775 sqm in January 2020. This reveals the construction sector' s sharp slowdown as few projects are undertaken amid the looming national uncertainty.

**Therefore, when properly scrutinized, the RE uptrend does not translate into "real growth terms" that can help uplift the economy.** In fact according to BLOMinvest, the economic growth in Lebanon was slashed to an estimated -7.4% in Q1 2020. The negative growth rate had further contracted from the -5.8% in Q1 2019, knowing that RE alone composes approximately 15% of Lebanon' s GDP while the Construction sector grasps an estimated 4% of GDP (CAS national accounts, 2018).

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